



# COMMISSION NEWS

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ARIZONA CORPORATION COMMISSION, 1200 W. WASHINGTON, PHOENIX, AZ 85007

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CONTACT: HEATHER MURPHY (602) 542-0844

## **ARIZONA CORPORATION COMMISSION CRACKS DOWN ON PROMISSORY NOTE FRAUD**

*—Joins 37 other states, the District of Columbia and the SEC in a coordinated action—*

PHOENIX — The Arizona Corporation Commission's Securities Division today joined other state and federal securities regulators in announcing a major crackdown on sellers of promissory notes. Promissory notes promise investors high returns and low risk. The notes, often sold by insurance agents, are in fact very risky and often fraudulent. Many victims are elderly. This effort highlights a serious and growing problem.

The following is a summary of recent Commission actions or orders involving promissory notes:

In a case filed today, the Commission alleges that a former securities salesman created a company that sold over \$500,000 in promissory notes to eight investors. The company subsequently defaulted on the notes, with the investors losing their investment.

In a case filed in March, the Division brought action against a Tucson-based insurance agent who sold 41 promissory notes to 16 Arizona investors, for a total investment of \$1,176,084.62. The promissory notes were from companies across the country, including several in which the principals have been indicted or convicted of fraud. The notes were supposed to pay 10 to 13% interest. The agent received commissions of \$109,121.71 for selling the notes.

In May 2000, the Commission ordered five individuals to return \$4,200,879 to investors. The five had sold fraudulent promissory notes to 93 investors, allegedly to raise money to collect a non-existent judgment against the

State of Arizona. These notes purportedly paid up to 200% interest.

In April 2000, the Corporation Commission ordered a Mesa company to offer to repay \$6,775,456.97 to 126 investors. The company sold the promissory notes to finance its business. The notes paid up to 60% interest. One of the company's salespeople had previously been barred by the Commission from selling securities, a fact that would have been revealed to investors if they had checked with the Commission prior to investing.

Responding to complaints about promissory notes, securities regulators in 37 states and the District of Columbia<sup>1</sup> formed a task force in May 1999. The North American Securities Administrators Association (NASAA), an association of state securities regulators of which the Commission is a member, coordinates the task force. This joint effort has resulted in 370 actions against 332 individuals and entities. In addition, the U.S. Securities and Exchange Commission announced numerous cases against marketers of promissory notes.

"Low interest rates are great for the economy but hard on people who rely on safe and predictable income from bank accounts, money market funds and dividends. This has provided an opportunity for frauds like we see with promissory notes," says Mark Sendrow, director of the Arizona Corporation Commission's Securities Division.

Arizona Corporation Commission Chairman, Carl Kunasek warns: "Investors are attracted to this type of investment because it has an aura of safety with a higher-than-market rate of return. Investors must never forget the first rule of finance: The higher the reward, the higher the risk. In today's market there's no such thing as a 'guaranteed' 10% or 15% return."

Commissioner Jim Irvin notes that "Promissory notes are often sold by independent life insurance agents—lured by high commissions—who may know nothing about the promoters of the investments beyond what they're told. The agents may not realize that they must be licensed as securities brokers with state securities regulators to sell securities." Commissioner Bill Mundell cautions that "Some notes are issued on behalf of companies that don't

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<sup>1</sup> Alabama, Arizona, California, Colorado, Connecticut, District of Columbia, Florida, Georgia, Idaho, Illinois, Indiana, Iowa, Kansas, Kentucky, Louisiana, Maryland, Massachusetts, Michigan, Mississippi, Missouri, Nebraska, New Jersey, New Mexico, New York, North Carolina, North Dakota, Ohio, Oregon, Pennsylvania, Rhode Island, South Carolina, Tennessee, Texas, Utah, Virginia, Washington, West Virginia and Wisconsin.

even exist and often are part of a Ponzi scheme.” Investors often get official looking promissory note certificates, complete with legal-sounding language and gold embossed seals. Many of these notes were purportedly bonded or guaranteed by non-licensed insurance companies located offshore.

The public is encouraged to “investigate before you invest” by contacting the Securities Division at (602) 542-4242, or toll free at 877-811-3878. Additional information can be obtained from NASAA’s web site at [www.nasaa.org](http://www.nasaa.org) and from the Division’s web site at [www.ccsd.cc.state.az.us](http://www.ccsd.cc.state.az.us).

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## SIDEBAR ARTICLE

### **HOW IS PROMISSORY NOTE FRAUD COMMITTED AND HOW CAN I PROTECT MYSELF?**

Promissory note fraud may work like this: A life insurance agent who sold you an annuity calls with an intriguing investment opportunity. A supposedly “well-established” company is looking to expand its business and needs capital. Instead of borrowing money from a traditional lender it is offering investors an opportunity to purchase “promissory notes,” typically with a maturity of nine months and an annual interest rate between 12% and 18%, far more than an investor could get elsewhere. Agents urge clients to “cash-in” their life insurance policies and “roll” them into fraudulent promissory notes. Investors usually end up losing their entire investment.

Here are some tips to protect yourself and your money:

- Before investing in any promissory note, investors should always check with their state securities regulator (602/542-4242) to confirm that the notes are properly registered or legally exempt from registration. If you cannot verify that the notes are registered or exempt from registration, hold onto your money. Do research to ascertain the legitimacy of the company whose notes are being offered.
- Agents selling these “notes” are usually required to be licensed by both the state and the National Association of Securities Dealers. To find out if the agents are registered or have a disciplinary

history, contact your state securities regulator or call the NASD Public Disclosure Hotline at 800-289-9999.

- Be suspicious if the notes have an above-market interest rate with a maturity of less than a year. With a one-year FDIC-insured bank certificate of deposit yielding a little over 6%, you should be very skeptical when someone offers you a nine-month "note" from an obscure firm promising 12%.

To check out an investment, contact the Securities Division at (602) 542-4242 or toll free at 877-811-3878. Additional information is available at the Securities Division web site at [www.ccsd.cc.state.az.us](http://www.ccsd.cc.state.az.us).

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